March 2, 2000

The Honorable Richard Lugar, Chairman
Senate Agriculture, Nutrition & Forestry Committee
United States Senate
Washington, D.C. 20510

The Honorable Phil Gramm, Chairman
Senate Banking Committee
United States Senate
Washington, D.C. 20510

Dear Chairmen Lugar and Gramm:

The Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC") are writing in response to your request that we present to Congress a report addressing the desirability of lifting the current prohibition on single stock futures together with any legislative proposals. This letter presents the current views of the SEC and the CFTC on these issues.

CFTC and SEC staffs have met numerous times to discuss the issues raised by your request and have worked diligently to formulate an appropriate response. Specifically, the discussions have focused on the statutory and regulatory changes needed to permit single stock futures contracts to trade in the U.S. in accordance with the following principles. The agencies agree that the solution should foster innovation in financial markets, maintain international competitiveness, encourage liquidity and transparency of trading, mitigate systemic risk, and assure high standards of investor and customer protection and market integrity. The agencies also believe that any proposal must maintain consistent oversight of stock, options, futures, single stock futures, and the markets and intermediaries that trade them. The framework for regulation of single stock futures should have the capacity to evolve to meet the changing needs of the marketplace. In developing a flexible system of joint regulation, the SEC and the CFTC should strive to avoid imposing any unnecessary costs or burdens or duplicative regulation on securities or futures markets or market participants.

Accordingly, we believe that any legislation in this area should empower the SEC and the CFTC to cooperate and coordinate their respective regulations to the extent practicable. CFTC and SEC staffs have discussed how the principles of shared regulation should be implemented. We agree that, to assure that these products can be offered broadly by both domestic securities and futures exchanges, legislation should authorize both the SEC and the CFTC to regulate: (i) single stock futures; (ii) intermediaries that offer single stock futures; and (iii) markets that list and trade single stock futures.

The SEC and the CFTC each recognize the significant interests of the other agency in administering their respective statutes and regulations with regard to single stock futures, and therefore, the SEC and the CFTC will endeavor to develop a framework under which each agency is fully able to satisfy its statutory mandate. CFTC and SEC staffs also have reached tentative agreement on initial standards for trading single stock futures such as harmonizing margin requirements, restricting dual trading, testing sales and supervisory personnel, and establishing uniform listing standards. In the area of insider trading, we have agreed that the

SEC would take the lead in detecting, deterring, and prosecuting insider trading involving single stock futures. In other areas, such as segregation of customer funds, Securities Investor Protection Corporation coverage, and application of the net capital rule, where regulation is recognized as being equivalent the agencies have agreed to avoid duplicative oversight.

The staffs have pursued the concept of "notice registration" for intermediaries and markets already registered with either the SEC or the CFTC. For example, a registered broker-dealer filing a form of notice registration with the CFTC would become a registered futures commission merchant ("FCM") for the sole purpose of offering single stock futures and be subject to the core provisions of the federal commodities laws for purposes of its activities relating to them. To avoid duplicative regulation, notice registration would allow already-registered intermediaries and markets to transact business in single stock futures without being required to go through the registration process under both the Securities Exchange Act of 1934 ("'34 Act") and the Commodity Exchange Act ("CEA"). For example, a registered FCM in good standing wishing to offer single stock futures to its customers would file with the SEC an appropriate form of notice registration that alerts the SEC to its new activities. The FCM would be able to commence those activities without an SEC order granting registration under Section 15 of the '34 Act.

We also are considering whether the agency accepting notice registration could defer to the "principal" regulator's equivalent regulation in areas such as inspections and examinations, books and records, audit trails, and disciplinary action against registrants. For example, in such areas, the principal regulator for a futures exchange or an FCM would be the CFTC, and for a securities exchange or a broker-dealer would be the SEC.

Nevertheless, intermediaries and markets that register through this process would be subject to certain "core provisions" of the regulatory scheme administered by the agency accepting notice registration. The agencies have not yet reached specific agreement on the scope or application of these core provisions. The CFTC and SEC staffs have, however, identified and discussed a variety of issues relating to trading single stock futures that may need to be addressed in a regulatory proposal, such as large trader reporting, customer suitability and disclosure requirements, and sales practices.

While these important issues remain unresolved, the agencies have agreed that they should develop a Memorandum of Understanding that implements the regulatory framework and a Coordinating Committee to address ongoing issues regarding shared regulation. The Memorandum of Understanding would provide a regulatory blueprint so that single stock futures could be traded on securities exchanges and futures exchanges by intermediaries currently regulated by only one agency, without undermining investor protection and the integrity of trading markets, without imposing unnecessary, duplicative regulation on markets or participants, and without promoting regulatory arbitrage.

The issues raised are complicated and require detailed statutory and regulatory solutions that will meet the goals of Congress, the President's Working Group on Financial Markets, and regulators. In addition, resolution of these issues must address the needs of the markets and market participants, protect investors, and provide an environment in which markets can continue to develop. The agencies agree to work diligently in the coming months to reach further consensus on the regulatory issues and to provide a comprehensive legislative proposal to your Committees in response to your request before Congress adjourns. Notwithstanding the many challenges that we face, we believe it is possible to craft a strong yet flexible regulatory framework for single stock futures.

Yours truly,

Arthur Levitt	William J. Rainer
Chairman	Chairman
Securities and Exchange Commission	Commodity Futures Trading Commission